ConsumersUnion
POLICY & ACTION FROM CONSUMER REPORTS

July 21, 2015

Secretary Thomas Perez
c/o Office of Regulations and Interpretations
Office of Exemption Determinations
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue, N.W.
Washington, D.C. 20210

Re: Conflict of Interest Rule, RIN 1210-AB32
Proposed Best Interest Contract Exemption, ZRIN: 1210-ZA25

Dear Secretary Perez:

Consumers Union, the advocacy division of Consumer Reports,[1] is pleased to submit comments on the Department of Labor's (DOL's) proposed conflict of interest rule. Where appropriate we have also included comments from consumers who have written to us about problems they have experienced when seeking investment advice. The proposed rule would significantly strengthen protections for consumers who are saving for retirement and those who want to retire with dignity knowing that their retirement income is secure. It would require financial advisers and their firms to provide retirement investment advice that is in the best interests of their clients rather than for their own financial gains. We urge the DOL to finalize and implement this rule as soon as possible.

Background

When consumers decide to leave a job or retire, they must decide what to do with the savings they have accumulated in their retirement plans. It is often at this point that many consumers realize they do not have the necessary financial expertise or tools to make important life changing decisions about how and where to invest their retirement savings. Many consumers turn to financial professionals for help in navigating the complex and often confusing world of financial investments. While many of these professionals commit to serving their clients' best interests, others may not. Because of gaps in current law governing retirement accounts, financial advisers are not required to make recommendations that are in their client's best interests. Advisers are allowed to

[1] Consumers Union is the public policy and advocacy division of Consumer Reports. Consumers Union works for a fair, just, and safe marketplace for all consumers and to empower consumers to protect themselves, focusing on the areas of telecommunications, health care, food and product safety, energy, and financial services, among others. Consumer Reports is the world's largest independent product-testing organization. Using its more than 50 labs, auto test center, and survey research center, the nonprofit organization rates thousands of products and services annually. Founded in 1936, Consumer Reports has over 8 million subscribers to its magazine, website, and other publications.

Consumers Union
Headquarters Office
101 Truman Avenue
Yonkers, New York 10703-1057
(914) 378-2029
(914) 378-2992 (fax)

Washington Office
1101 17th Street N.W. # 500
Washington DC 20036
(202) 462-6262
(202) 265-9548 (fax)

West Coast Office
1535 Mission Street
San Francisco, CA 94103-2512
(415) 431-6747
(415) 431-0906 (Fax)

South West Office
506 W. 14th, Suite A
Austin, TX 78701-1723
(512) 477-4431
(512) 477-8934 (fax)

give imprudent and disloyal advice, steer plans and Individual Retirement Account (IRA) owners to investments based on their own, rather than their customers' financial interests, and to ignore conflicts of interest in ways that would be prohibited if the same people were held to the standard of fiduciaries.

The cost to retirement saving of conflicted advice is staggering. Based on the best data available, the DOL estimates that investors will lose somewhere between $210 billion and $430 billion over 10 years and between $500 billion and $1 trillion over 20 years as a result of conflicted advice with respect to mutual fund investments in IRAs. In addition, a retirement saver who moves money out of a 401(k) plan into an IRA based on conflicted advice can expect to lose 12 to 24 percent of the value of his or her savings over 30 years.

The proposed investor protection rule would update the fiduciary standard under our pension rules. It covers advice to traditional and defined contribution pension plans, such as 401(k) plans, as well as advice to plan participants and to those who save through IRAs. It clarifies and expands who, as a result of giving investment advice, is a fiduciary of an employee benefit plan under the Employee Retirement Income Security Act (ERISA). It would require financial advisers to be held to a fiduciary standard of putting their clients' interests first and foremost, free of conflict and subject to liability for harm resulting from conflicted advice they may provide. Advisers would no longer be allowed to profit from the advice they give, while their clients lose millions from unnecessary fees and low returns.

We support many of the provisions in the rule, most notably:

- Updating current retirement rules to reflect the modern financial marketplace where financially unsophisticated consumers are required to manage their own retirement savings;

- Protecting consumers from conflicted advice when they are steered into inappropriate investments that benefit the adviser but not the consumer;

- Requiring best interest contracts that would hold advisers and their firms liable for any losses that result from a breach of contract;

- Requiring advisers to provide important point-of-sale and on-going disclosures showing the true costs consumers pay for investment advice upfront and over time; and

- However, while the rule would give consumers much needed protections when seeking retirement advice, it is not perfect. We strongly oppose the inclusion of pre-dispute mandatory arbitration clauses in the consumer contracts. We urge

Consumers Union
Headquarters Office
101 Truman Avenue
Yonkers, New York 10703-1057
(914) 378-2029
(914) 378-2992 (fax)

Washington Office
1101 17th Street N.W. # 500
Washington, DC 20036
(202) 462-6262
(202) 265-9548 (fax)

West Coast Office
1535 Mission Street
San Francisco, CA 94103-2512
(415) 431-6747
(415) 431-0906 (Fax)

South West Office
506 W. 14th, Suite A
Austin, TX 78701-1723
(512) 477-4431
(512) 477-8934 (fax)

DOL to strengthen the protections against use of these clauses and against forced waivers of class action rights.

I. Current rules need to be updated to reflect the modern financial marketplace where unsophisticated consumers are required to manage their own retirement accounts.

When the fiduciary rule under ERISA was first promulgated in 1975, the retirement landscape looked very different from today's ever evolving financial marketplace. At that time, most consumers invested their retirement savings in defined-benefit plans or traditional pension plans. IRAs had just been created, and 401(k)'s didn't even exist. Consumers didn't need personalized investment advice, because their retirement savings were already being professionally managed for them through their employers. Regulators didn't take into account how the rule would affect financially unsophisticated individual consumers responsible for making their own decisions about how to invest their retirement savings.

Gaps in the rule do not require advisers to act in the best interest of the client when one-time or periodic advice is given. The current rule only applies when there's a "mutual agreement" that the advice will be the "primary basis" for the investment decision. This requirement can easily be circumvented with fine print and legalese. In addition, the current rule does not apply to recommendations to roll over from a defined benefits plan into a self-directed IRA, one of the most important financial decisions many people will ever make.

We support the DOL's updates to the ERISA rule. Under the proposed rule, anyone (including brokers, registered investment advisers, insurance agents, or other type of adviser) who provides individualized investment advice to retirement savers whether they are saving through a traditional or defined contribution plan such as an IRA or 401(k), would be a fiduciary and required to provide best interest advice. Being a fiduciary creates a legal relationship of trust and requires the adviser to provide impartial advice and, with carefully specified exceptions, not accept any payments for that advice that would create a conflict of interest. The rule allows for conflicted compensation but requires that advisers who receive conflicted compensation to enter into a contract with their customers in which they acknowledge their fiduciary status and commit to giving advice that is in the customer's best interest despite the conflicted compensation.

The rule would specifically eliminate the outdated "regular basis" loophole that allows advisers to provide one-time or episodic advice without being subject to a fiduciary standard. It also would close the "mutual agreement" and "primary basis" loopholes that allow advisers and their firms to evade the fiduciary standard. These updates are long overdue and will go a long way in securing the nest eggs consumers have spent a life-time building up.

Finally, the rule appropriately carves out education from its definition of retirement advice. This would allow firms and financial advisers to provide general educational information and materials to consumers without being subject to a fiduciary duty -- as long as that information does not contain any specific investment recommendations that consumers can reasonably be expected to act upon.

II. The rule would protect consumers from conflicted advice where they are steered into inappropriate investments that benefit the adviser but not the consumer.

Jeanne, Dudley, MA

"I invested a large part of a $70,000 inheritance with a private financial advisor recommended by a family friend. I know absolutely nothing about investments. He constantly changed the investment each time paying himself a fee, I too late realized. When I finally learned that he had moved from the Massachusetts area to Florida, he had earned more money than I had."

Being personally responsible for one's own retirement investments comes with a lot of challenges. Consumers are faced with a multitude of complex and confusing decisions. They must decide how much to save, what types of retirement accounts they should use, and which products are best for them depending on their unique features, costs, benefits, and risks. Consumers often do not have the information, expertise or tools to make informed investment decisions about what is best for them. Many are forced to rely on the advice of professional advisers.

Because some advisers do not put their clients' interests first, they can freely steer those clients into excessively high- cost, and low-performing investments that drain their hard-earned savings while at the same time, increasing the advisers' profits. The compensation advisers receive for giving such advice, works against consumers. If an adviser is paid based on the products the adviser sells, and selling one product makes the adviser an 8 percent commission instead of another product that makes the adviser a 3 percent commission, the adviser may rationalize recommending the product with the 8 percent commission. And, if the adviser's firm is pressuring the adviser to hit specific sales quotas for selling the product with the 8 percent commission, and bases the adviser's compensation and bonus on hitting certain sales goals for that product, it creates conflicts that even the most ethical adviser would have difficulty avoiding. Many consumers may not know that their retirement savings are being slowly and deliberately drained because of these conflicts. The conflicts can be well hidden and are likely to result in excessive fees and low performing investments. Without adequate safeguards, retirement savers will remain at risk of being harmed by conflicted advice that is a direct result of skewed incentives and, sometimes, just plain greed.

III. Consumer Contracts – If the firm or adviser breaches any of the terms of the Best Interest Contract Exemption (BICE), the retiree can hold them liable for any losses that resulted from the breach.

Arthur, Charlestown, WV

"The issue I have is that there is no recourse, no accountability for bad advice/recommendations in this field. ...They [financial advisers] should have to forfeit their fees if they lose for their clients."

Perhaps the most important feature of the proposed rule is the Best Interest Contract Exemption (BICE), which would provide important protections for consumers from conflicted advice in a manner that would allow advisers and their firms to collect commissions and other sales-related compensation. The broker-dealer business model would be preserved. To qualify for the BICE, advisers and firms would be required to contractually agree that any recommendations that they provide are in their client's best interest, without regard to their own financial or other interests. This would mean providing advice that a prudent and impartial expert would provide under the same circumstances. In addition, the fees that firms and advisers charge must be reasonable in light of the services that they provide.

We also support the proposed rule's requirement that firms adopt policies that are reasonably designed to minimize the harmful impact of any conflicts of interest. Firms would remain free to recommend proprietary or in-house products but could no longer set quotas for the sale of such products and base bonuses on their success in meeting those quotas. Similarly, while firms would be free to pay their advisers more to sell certain investments, those differential payments would have to be based on neutral and objective factors, such as the amount of time necessary to research and implement the investment strategy.

If firms or advisers breach any of the contractual provisions, the consumers would be able to hold them liable for any losses that resulted from the breach. We believe that having a mechanism to hold firms and advisers accountable will induce advisers and firms to compete better on cost and quality rather than focus on how much they stand to profit from their advice.

IV. Advisers would be required to make important point-of-sale and on-going disclosures showing the costs that retirement investors are paying

Joe, Memphis, TN

"Retirement money should be saved not gambled. And the hidden fees should not be hidden only for you to find out later that you owe half or more to the adviser."

Consumers Union
Headquarters Office
101 Truman Avenue
Yonkers, New York 10703-1057
(914) 378-2029
(914) 378-2992 (fax)

Washington Office
1101 17th Street N.W. # 500
Washington DC 20036
(202) 462-6262
(202) 265-9548 (fax)

West Coast Office
1535 Mission Street
San Francisco, CA 94103-2512
(415) 431-6747
(415) 431-0906 (Fax)

South West Office
506 W. 14th. Suite A
Austin, TX 78701-1723
(512) 477-4431
(512) 477-8934 (fax)

We also support the point-of-sale and on-going disclosures required by the rule. These disclosures will give consumers vital information about the long-term costs they are likely to pay for the advice received. This will give them the information needed to more effectively compare costs and services. Conflicts of interests like hidden fees that are often buried in the fine print, or kickbacks for selling certain investments, must be clearly and prominently disclosed -- and in some instances may be strictly forbidden. Consumers will also be able to see and understand the impact that costs can have on their retirement portfolios over the long-term. If firms or advisers breach any of these contractual provisions, retirement savers can hold them liable for any losses that resulted from the breach.

V. We strongly oppose the inclusion of pre-dispute mandatory arbitration clauses in the consumer contracts.

Under the proposed rule, contracts between investment advisers and consumers can require that individual disputes be handled through arbitration. We oppose this practice. A fundamental protection for consumers is the right to hold wrongdoers accountable under the law. This right is undermined when consumers are forced to give up their right to take their complaint to court and instead are required to go through forced arbitration. The arbitration process is often set up by the financial firm. It lacks many of the fundamental protections of an established legal process, and can be unfairly skewed against consumers in favor of the financial firm. Pre-dispute mandatory arbitration clauses should not be allowed in these consumer contracts. Consumers should have the right to bring their complaints to court.

Forced arbitration clauses also often restrict consumers from joining together with others who have been mistreated in the same way, by the same company, to bring a class action against the company. Without the ability to bring a class action, the cost of pursuing an individual claim is too high and often results in the wrongdoer being let off the hook.

The proposed rule would require that contracts between retirement investment advisers and consumers preserve the right of consumers, who have been harmed by a breach of the fiduciary standard, to bring a class action in court. We fully agree that in situations where the adviser is committing the same kind of breach of duty against multiple consumers, allowing those consumers to join together in a class action is important. It makes the legal system a more effective means for consumers to recover damages and a more effective deterrent against an adviser's carelessness and misconduct. We strongly support this goal and the inclusion of this requirement in the rule. However, as the DOL notes, this requirement is modeled after FINRA rules. The FINRA requirement has been challenged in court, and the Second Circuit ruled just last month that the FINRA requirement does not prevent forced class action waivers from being inserted in contracts and being enforced. Cohen v. UBS Financial Services, Inc., Docket No. 14–781–cv. (2d Cir. June 30, 2015).

Moreover, there is substantial evidence that consumers may "win" FINRA arbitrations but receive significantly less than they deserve. For example, a study analyzing 14,000 FINRA arbitration awards over a ten-year period found that investors with significant claims suing major brokerage firms could expect to recover only 12 percent of the amount claimed.[2] There is also evidence that brokers are easily able to expunge their records of consumer complaints, as if they never occurred.[3] In addition, arbitrators are not required to explain their decisions and their decisions are virtually impossible to appeal. The result is an opaque, unfair process that benefits the brokerage industry, not consumers.

We continue to support legislation to protect consumers' right to bring claims in court rather than being forced to rely on binding private arbitration, and their right to bring a class action in accordance with long-established procedures. We urge the DOL to look for a more effective way to safeguard these rights for consumers in its rule and to avoid including any provisions or statement that could be used to reinforce or acquiesce in any restriction on these important rights.

Conclusion

We appreciate the DOL's hard work and thoughtful approach in developing a proposed rule that would require financial advisers to put their clients' interests first rather than their own when providing retirement investment advice. The harm that consumers suffer as a result of conflicts of interest can profoundly impact their quality of life during retirement, including where someone will live, whether they will be able to afford the necessities of life, and whether they can remain independent. Once their retirement funds are gone, they may not have the time, ability or opportunity to rebuild. They deserve more. They have worked a lifetime for more.

We urge the DOL to finalize and implement this rule as soon as possible.

Sincerely,

Pamela Banks

Pamela Banks
Senior Policy Counsel
Consumers Union

---

[2] Edward S. O'Neal, Ph.D. and Daniel R. Solin, Mandatory Arbitration of Securities Disputes — by Edward S. O'Neal, Ph.D. and Daniel R. Solin1 A Statistical Analysis of How Claimants Fare, Securities and Litigation and Consulting Group, June 2007, http://bit.ly/1LtUCgU.

[3] Susan Antilla, *A Murky Process Yields Cleaner Professional Records for Stockbrokers*, NEW YORK TIMES DEALBOOK, September 25, 2014, http://nyti.ms/1uqiwyn.

ConsumersUnion
POLICY & ACTION FROM CONSUMER REPORTS

Consumers Union
Headquarters Office
101 Truman Avenue
Yonkers, New York 10703-1057
(914) 378-2029
(914) 378-2992 (fax)

Washington Office
1101 17th Street N.W. # 500
Washington DC 20036
(202) 462-6262
(202) 265-9548 (fax)

West Coast Office
1535 Mission Street
San Francisco, CA 94103-2512
(415) 431-6747
(415) 431-0906 (Fax)

South West Office
506 W. 14th, Suite A
Austin, TX 78701-1723
(512) 477-4431
(512) 477 8934 (fax)